

Judicial Foreclosures and Their Discontents

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I. INTRODUCTION

The nation is currently divided regarding whether, and to what extent, judicial process is deemed necessary for a mortgage loan holder to foreclose on property secured by a defaulted mortgage loan. Foreclosure actions are creatures of state law, and the states have produced many responses to this issue along a spectrum of differing policy commitments.

In roughly half of the states, a foreclosure action is a perfunctory administrative proceeding without any judicial element. If a borrower desires judicial process, the borrower must file a lawsuit against the mortgage holder or servicer to stop the non-judicial foreclosure proceeding. If a borrower does not file a lawsuit to stop the foreclosure proceeding, the property could be sold at auction in as little as six weeks.

By contrast, in so-called judicial foreclosure states, the mortgage holder must file a lawsuit to foreclose on the mortgaged property. At the same time, however, such “judicial” foreclosures contain an increasing number of administrative components, particularly mandatory mediation programs, which creates a situation in which a judicial foreclosure lasts for years, even when the borrower does not respond to the complaint.¹

Even in judicial states, the courts are ambivalent when it comes to determining the relative mix of judicial process and administrative procedure necessary in a foreclosure proceeding. By varying degrees, courts in judicial states view foreclosure actions as ordinary lawsuits or as unique proceedings that contain both judicial and administrative elements. This type of ambivalence in judicial foreclosures is becoming more pronounced the more foreclosures are filed and the more the judicial foreclosure process is scrutinized, leading to disagreement among courts and attorneys regarding how a foreclosure action should proceed.

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¹In judicial states such as New York and Florida, the average foreclosure action lasts between two and three years. See Les Christie, *Foreclosure Free Ride: 3 Years, No Payments*, CNNMONEY (Jan. 1, 2012, 4:40 PM), http://money.cnn.com/2011/12/28/real_estate/foreclosure/index.htm. Contested foreclosures and/or those involving mandatory mediation programs could last considerably longer before resolution.

II. EXAMPLES OF JUDICIAL FORECLOSURE AMBIVALENCE

Two separate splits have emerged in authority among the intermediate appellate courts in Ohio—a prominent judicial foreclosure state. In one such split, the appellate courts are divided regarding whether a mortgage assignment must be executed in favor of the foreclosure plaintiff before the foreclosure action is filed, or simply whether the mortgage assignment must be executed before the foreclosure plaintiff moves for judgment.² The courts requiring the assignment of mortgage before judgment tend to view a foreclosure action as an ordinary lawsuit under which the Ohio equivalent of Federal Rule 17(a) applies.³ This rule permits assignees to sue in their own names where it is sufficient for the plaintiff simply to allege that it is entitled to enforce the promissory note and accompanying mortgage deed before it moves for default or summary judgment.⁴

On the other hand, the Ohio appellate courts that require a mortgage assignment to be executed in favor of the mortgagee before the complaint is filed tend to view the foreclosure action as more of an administrative, even inquisitional process. Under this approach, the mortgagee must produce documentation sufficient to illustrate to the court that the action has been brought by the actual party entitled to enforce the mortgage loan, even before the borrower has had an opportunity to respond to the complaint. In order to advance the foreclosure action to judgment and sale, such sufficient documentation must be produced, or the case will be dismissed, albeit without prejudice.⁵

Additionally, a recent split has emerged regarding the effect of a Rule 41 voluntary dismissal on a foreclosure judgment and unconfirmed foreclosure sale. An Ohio intermediate appellate court, the state's Second District Court of Appeals, viewed a foreclosure action more as an ordinary lawsuit than a hybrid proceeding when it held that a Rule 41 voluntary dismissal had no effect on the existing judgment, which could only be vacated upon a meritorious Rule 60 motion.⁶

By contrast, a different appellate court nevertheless held that a Rule 41 voluntary dismissal could be filed after a judgment and a foreclosure sale, dissolving the action and vacating the judgment and sale with a simple notice

² See *Fed. Home Loan Mortg. Corp. v. Schwartzwald*, 957 N.E.2d 790, 802–03 (Ohio Ct. App. 2011). This case is currently a certified conflict case before the Ohio Supreme Court. 954 N.E.2d 661 (Ohio 2011) (table).

³ FED. R. CIV. P. 17(a); OHIO CIV. R. 17(a).

⁴ See, e.g., *U.S. Bank Nat'l Ass'n v. Marcino*, 908 N.E.2d 1032, 1036 (Ohio Ct. App. 2009).

⁵ See, e.g., *Wells Fargo Bank, Nat'l Ass'n v. Byrd*, 897 N.E.2d 722, 724, 727 (Ohio Ct. App. 2008).

⁶ *Coates v. Navarro*, Nos. 86-CA-11 and 86-CA-18, 1987 WL 8490, at *5 (Ohio Ct. App. Mar. 27, 1987).

filing and without any motion or approval by the court or the opposing parties.⁷ In this respect, the Ohio Sixth District Court of Appeals has viewed the foreclosure sale process as an integral part of a foreclosure action, rather than merely as a form of execution upon a judgment obtained against the borrower.⁸

Consistent with this holding, the same appellate court recently revealed another instance of the ambivalence between administrative and judicial elements in the judicial foreclosure process, explaining that:

Although appellants are correct in stating that an order of foreclosure is a final and appealable order, and that at least one Ohio appellate court has held that Civ.R. 60(B), and not Civ.R. 41(A), provides the only mechanism to change such an order, this court has taken the position that a foreclosure action, with its two-part process, *is a unique process under the law* and that prior to completion of both parts of that process—that is, completion of both the order of foreclosure and the order confirming the sheriff's sale—an entire foreclosure action, including any previously-issued order of foreclosure, can be dissolved with the filing of a Civ.R. 41(A) voluntary dismissal.⁹

Both cases contain incongruities that further underscore this ambivalence in judicial foreclosures. In *Coates v. Navarro*, an Ohio appellate court held that only a meritorious motion for relief from judgment under the state's Rule 60(B) could dissolve the judgment.¹⁰ However, it is strange, to say the least, that the party who received a favorable judgment would move to vacate, or receive relief from, the same judgment. This is particularly so because one of the necessary elements in moving to vacate a judgment under Ohio Rule 60(B) is to establish a meritorious defense or claim to assert if relief is granted, implying that justice may be denied if the movant is denied an opportunity to assert such a meritorious claim or defense.¹¹ However, if a party is moving to vacate its own judgment, it is not doing so to litigate any claims or defenses which have already been resolved in its favor. Instead, such a party is moving to vacate the judgment in order to dismiss the action.

⁷ Compare OHIO R. CIV. P. 41(A)(1) (permitting a plaintiff to dismiss all claims either by "filing a notice of dismissal at any time before the commencement of trial unless a counterclaim" is pending, or by "filing a stipulation of dismissal signed by all parties who have appeared in the action"), with FED. R. CIV. P. 41(a)(1)(A) (notice of voluntary dismissal must be filed "before the opposing party serves either an answer or a motion for summary judgment" or by party stipulation).

⁸ See *Countrywide Home Loans Servicing v. Nichpor*, No. WD-11-047, 2012 WL 929023, at *2 (Ohio Ct. App. Mar. 16, 2012); *N. Ohio Inv. Co. v. Yarger*, No. WD-06-025, 2006 WL 2587454, at *3 (Ohio Ct. App. Sept. 8, 2006).

⁹ *Countrywide*, 2012 WL 929023, at *2 (emphasis added) (citations omitted).

¹⁰ *Coates*, 1987 WL 8490, at *5.

¹¹ See *GTE Automatic Electric, Inc. v. ARC Indus., Inc.*, 351 N.E.2d 113, 113 (Ohio 1976).

By contrast, as in *Countrywide Home Loans Servicing v. Nichpor* and *Northern Ohio Investment Co. v. Yarger*,¹² some Ohio appellate courts, in viewing the foreclosure proceeding as a hybrid proceeding involving both administrative and judicial elements, appear to have no answer for some procedural issues created by this approach. If a judgment may be vacated when the foreclosure plaintiff files a voluntary notice of dismissal under Rule 41, it is not clear what effect such a filing would have on the opposing party's appellate rights. Additionally, if a third party purchases the property at a sheriff's sale, and the mortgagee suffers prejudice as a result of the third party's purchase,¹³ then a mortgagee could simply file a voluntary dismissal notice to dissolve the effects of the sale before the sale is final and a new deed is issued in favor of the third party. In non-foreclosure lawsuits, judgments are not so fungible.

III. JUDICIAL FORECLOSURE AMBIVALENCE CURRENTLY

Judicial foreclosure ambivalence has become more recognizable and pronounced in the wake of the housing crisis. The most obvious contributing factor is the current glut of foreclosure cases that has accumulated over the past several years and that will likely remain high for many years to come. Another significant factor causing judicial ambivalence is the documentation issues and scandals involving the mortgage servicing industry, such as the "robo-signing" scandal in which affiants employed by mortgage servicers may not have executed affidavits with the requisite personal knowledge, despite attestations to the contrary.¹⁴ These factors have induced key players in judicial foreclosures—the courts, the litigators, and the parties—to transform a traditionally simplistic, almost mechanical process into one involving ever-increasing complexity and considerable disagreement on key issues.

As to the administrative components of a judicial foreclosure action, two significant issues have emerged. One issue is the substantial role mandatory mediation programs have played in the foreclosure process. Mandatory mediation programs have greatly increased the length of time it takes to resolve foreclosure disputes. Not surprisingly, as court dockets have become clogged with foreclosures, and tax revenues have declined, mediation resources have

¹² *Nichpor*, 2012 WL 929023; *Yarger*, 2006 WL 2587454.

¹³ A mortgagee's failure to outbid a third party could create liability for the mortgagee in certain ways. For one, the mortgagee may be required to bid the entire debt amount, regardless of the value of the property, in order to recover mortgage insurance proceeds that are tied to the price paid at a sheriff's sale. This is particularly the case for loans insured by the federal government through the Department of Housing and Urban Development. Additionally, if the mortgagee fails to enter a bid, and the property sells for a price far below the amount for which the mortgagee could hope to liquidate the property, the mortgagee will suffer a loss.

¹⁴ *Cf. Ohio v. GMAC Mortg., LLC*, 760 F. Supp. 2d 741, 743–44 (N.D. Ohio 2011) (alleging GMAC's practice of filing false affidavits is fraud in violation of the Ohio Consumer Sales Practice Act).

become strained.¹⁵ In Cook County, Illinois, a borrower who requests mediation once a foreclosure action is filed may not attend the first of several mediation conferences for nearly eight months.¹⁶ From that point, it is not uncommon for a case to be in mediation for over a year, during which time the foreclosure action is stayed.

This result is particularly vexing given that the longer a mortgage loan remains in default, the more difficult it is for the mortgagor to bring the loan current. The reason for this problem is not simply the accumulation of interest on the loan, but also the fact that the mortgage servicer ordinarily advances the costs for property taxes, hazard insurance, and mortgage insurance, including attorney fees and court costs—all of which are assessed to the borrower under the mortgage deed as a consequence of the borrower's default.¹⁷ Furthermore, mortgage loan servicers, who are tasked with determining whether a borrower receives a loan modification, are typically legally bound not to waive principal or interest on a loan—a reality that keeps loan balances exceedingly high relative to the values of the properties, thereby increasing the risk of a borrower's strategic default. The extreme delays occasioned by mandatory mediation also create additional risks for “charged off” properties¹⁸ and therefore make pursuing a foreclosure action financially unappealing to a mortgagee. Of course, the risk of abandoned properties increases for the same reasons.

Additionally, as the result of the “robo-signing” scandal, some courts have become skeptical of mortgagees and the documents filed with the court.¹⁹ These

¹⁵ See Alon Cohen, *New Source of Mortgage Mediation Funds: Seeing Success, States Are Adding and Expanding Mortgage Foreclosure Mediation Programs—Something the State AG Settlement Should Support*, CENTER FOR AMERICAN PROGRESS (May 17, 2011), http://www.americanprogress.org/issues/2011/05/mortgage_mediation.html.

¹⁶ See Anna C. Kahriman, *Cook County's Mortgage Foreclosure Mediation Program: One Year Later*, POSTESTIVO & ASSOCIATES, P.C. (July 27, 2011), http://www.potestivolaw.com/index.php?area=Articles&article_id=228.

¹⁷ Uniform covenants in the mortgage forms issued by the Federal National Mortgage Association (Fannie Mae) and Federal Home Loan Mortgage Corporation (Freddie Mac) permit a lender to “do and pay” for all “reasonable or appropriate” expenses arising out of a borrower's default, including property taxes, hazard insurance premiums, and property preservation costs that ultimately become a part of the borrower's balance due and owing. See, e.g., Security Instruments: First Lien Security Instruments, FREDDIE MAC, <http://www.freddiemac.com/uniform/unifsecurity.html> (follow “Form 3036: Ohio Mortgage” hyperlink; then view § 9).

¹⁸ “Charged off” properties are properties that have declined in value to such an extent that it no longer becomes financially worthwhile for mortgagees to bear the costs of pursuing foreclosure when the property will be liquidated at such a low price on a far-off date in the future.

¹⁹ See *Wash. Mut. Bank v. Phillip*, No. 16359/08, 2010 WL 4813782, at *2 (N.Y. Sup. Ct. Nov. 29, 2010) (quoting Chief Judge Lippman, who said “[w]e cannot allow the courts in New York State to stand by idly and be party to what we now know is a deeply flawed process, especially when that process involves basic human needs—such as a family home—during this period of economic crisis.”).

courts now demand compliance with increasing administrative requirements before a foreclosure action can be filed or before judgment can be granted in favor of the mortgagee. For instance, foreclosure actions in New York can only be permissibly filed with an affidavit from the mortgagee's counsel verifying both that the attorney communicated with the mortgagee's representative who reviewed the mortgage documents for accuracy, and that the attorney determined the documents contained no false statements of law.²⁰ New Jersey and a few Ohio counties have enacted similar requirements.²¹

In these instances, the courts are not viewing the foreclosure process as an ordinary lawsuit involving an adversarial process. Instead, these courts have transformed an ordinary judicial process into an inquisitorial proceeding in which the court is inquiring into the attorney-client relationship between the mortgagee and its counsel, and is requiring that the mortgagee's attorney effectively become a witness in the case. Such a requirement would be unheard of in the context of other civil lawsuits.

Besides additional administrative requirements, judicial foreclosures have seen changes to the actual judicial process. Most prominent among these changes are pre-trial litigation issues at the pleading and summary judgment stages. Many of these issues concern what remains the most contested factual issue in foreclosures, in either the judicial or non-judicial context: the foreclosing party's standing or status as the real party in interest to initiate a foreclosure action. This single issue creates problems at every stage of litigation from pleading to appeal. Additionally, and in the wake of the recent "robo-signing" scandal, the judgment stage, with its dependence on affidavits from mortgage loan holders, has become a particularly notable area for emerging issues.²² Not surprisingly, the two issues—standing and suspect affidavits—frequently arise at the same time.

As a matter of substantive law, few would deny that an originating mortgage lender has the right to assign or transfer the mortgage loan to another

²⁰ See Press Release, New York State Unified Court System, New York Courts First in Country to Institute Filing Requirement to Preserve Integrity of Foreclosure Process (Oct. 20, 2010), *available at* www.courts.state.ny.us/press/pr2010_12.shtml.

²¹ See Press Release, Notice to the Bar, Emergent Amendments to *Rules* 1:5-6, 4:64-1 and 4:64-2, Administrative Office of the New Jersey Courts (Dec. 20, 2010) (on file with the author); STEPHEN R. BUCHENROTH, AMERICAN BAR ASSOCIATION, OHIO COURTS REACT TO ROBO-SIGNERS BY PLACING BURDEN UPON LAWYERS (June 2011), *available at* http://www.americanbar.org/content/dam/aba/publications/rpte_ereport/2011/2011_aba_rpte_ereport_03_rp_buchenroth.authcheckdam.pdf (reacting to the two largest Ohio counties' decision to require plaintiff's lawyers to certify the accuracy of facts and documents in residential foreclosure cases).

²² See, e.g., *Bank of N.Y. Mellon Trust Co. Nat'l v. Mihalca*, No. 25747, 2012 WL 473925, at *3-4 (Ohio Ct. App. Feb. 15, 2012) (reversing summary judgment in favor of the mortgagee when an affidavit in support of Rule 56 motion was not sufficiently made on basis of personal knowledge and the conclusory testimony from mortgagee's representative that mortgagee was the holder of the mortgage was insufficient to satisfy mortgagee's initial burden under Rule 56).

party. Indeed such a practice forms the foundation on which most mortgage loans are originated and increases the funding available to issue additional mortgage loans.²³ However, the applicable law determining both the standards for transfers, and the rights and obligations of the parties, remains unclear. Most notably, it is not clear whether a promissory note secured by a mortgage deed is a negotiable instrument, sufficient to trigger Article III of the Uniform Commercial Code (UCC).²⁴ The typical mortgage deed contains so many terms and conditions that the promissory note may not function as a negotiable instrument, which is described as a “courier without luggage.”²⁵ Equally uncertain is whether Article IX of the UCC applies or whether state common law applies to such transfers.²⁶ Finally, some states rely upon documents, such as collateral mortgage assignments, to determine whether the foreclosure plaintiff is the proper party to commence the foreclosure action, and may not stress the role of the UCC at all.²⁷

Precisely how these substantive issues play themselves out in the context of Rule 12 and 56 motions is beyond the scope of this Article. However, needless to say, the uncertain legal and factual landscape with respect to this single substantive issue is creating its fair share of litigation.

IV. CONCLUSION

The pronounced forms of ambivalence in judicial foreclosures may or may not result in a more coherent rationale for the degree to which judicial process is deemed necessary before a foreclosure sale can occur. Across the nation, the difference of opinion on the topic is wide. At the same time, the current situation with judicial foreclosures has created increasing complexity in and greater scrutiny of the judicial foreclosure process. What had long been a mechanical practice has become a fresh source of intriguing legal issues relating to the nature and purpose of a foreclosure action.

²³ Such mortgage loans include those made under the auspices of the Government Sponsored Entities (GSEs), such as the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Corporation (Freddie Mac), not to mention federal government agencies that directly back mortgages, such as the Fair Housing Administration’s division within the Department of Housing and Urban Development.

²⁴ See Ronald J. Mann, *Searching for Negotiability in Payment and Credit Systems*, 44 UCLA L. REV. 951, 968–73 (1997).

²⁵ *Id.* at 978.

²⁶ See Jeffrey T. Ferriell, Professor, Capital Univ. Law Sch., Presentation at the Columbus Bar Association: Situation Overview—The Present State of the Law of Foreclosures (Sept. 30, 2011) (on file with author).

²⁷ See, e.g., *Fed. Home Loan Mortg. Corp. v. Schwartzwald*, 957 N.E.2d 790, 801 (Ohio Ct. App. 2011).